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No. 420

IN THE

Supreme Court of the United States

OCTOBER TERM 1959

LEATHERHIDE INDUSTRIES, INC.,

Petitioner,

-against-

SIDNEY LIEBERMAN,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

To the Honorable Chief Justice of the United States and the Associate Justices of the Supreme Court of the United States:

Your petitioner, Leatherhide Industries, Inc., respectfully prays for a writ of certiorari to the United States Court of Appeals for the Second Circuit, to review a determination of that Court rendered on June 29th, 1959, affirming order of the United States District Court for the Southern District of New York (192-204)* which order dismissed petitioner's petition for reorganization pursuant to Chapter X of the Act of Congress relating to Bankruptcy.

On August 26, 1959, petitioner duly applied to the Court of Appeals for rehearing, which application was denied on August 28, 1959.

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* Appeal was heard on original papers and numbers in parentheses refer to Record on Appeal.

Opinions Below

1. The opinion of the Court of Appeals is set forth in the appendix, *infra*.

2. The District Judge rendered no opinion.

3. Previous opinion of the Court of Appeals reversing a previous order of the District Judge is set forth in 261 F. 2d 560 (2nd Cir. Nov. 20, 1958). The District Judge wrote no previous opinion.

4. No opinion was rendered on the petition for rehearing.

Jurisdiction

The judgment of the Court of Appeals was entered on the 29th day of June, 1959. Application was made to that Court for rehearing, and denied on August 28, 1959. The jurisdiction of this Court is invoked under 28 United States Code, Section 1254(1).

Statutes Involved

The Statutes involved are as follows:

11 United States Code, Sections 541, 546, 567 and 569, reading as follows:

Sec. 541. *Petition of debtor.* Upon the filing of a petition by a debtor, the judge shall enter an order approving the petition, if satisfied that it complies with the requirements of this chapter and has been filed in good faith, or dismissing it if not so satisfied.

Sec. 546. *Good faith of petition.* Without limiting the generality of the meaning of the term "good faith," a petition shall be deemed not to be filed in good faith if—

(1) the petitioning creditors have acquired their claims for the purpose of filing the petition; or

(2) adequate relief would be obtainable by a debtor's petition under the provisions of chapter 11 of this title; or

(3) it is unreasonable to expect that a plan of reorganization can be effected; or

(4) a prior proceeding is pending in any court and it appears that the interests of creditors and stockholders would be best subserved in such prior proceeding.

Sec. 567. *Powers and duties; trustee.* The trustee upon his appointment and qualification—

* * * * * *

(6) shall give notice to the creditors and stockholders that they may submit to him suggestions for the formulation of a plan, or proposals in the form of plans, within a time therein named.

Sec. 569. *Preparation, filing, and hearing on plan; trustee appointed.* Where a trustee has been appointed the judge shall fix a time within which the trustee shall prepare and file a plan, or a report of his reasons why a plan cannot be effected, and shall fix a subsequent time for a hearing on such plan or report and for the consideration of any objections which may be made or if such amendments or plans as may be proposed by the debtor or by any creditor or stockholder.

Questions Presented

1. Was there any justification for the ruling that reorganization of the petitioner was not sought in good faith?

2. Was not the inability of petitioner to obtain relief under Chapter XI a compelling additional ground for initial approval of the petition?

3. Was there any justification for the inference of the District Court that reorganization necessarily involved a public sale of stock?

4. Did the District Court err in deciding the issues prior to the hearing of witnesses?

5. Did the District Court err in failing to direct notice of hearing to all creditors, stockholders of petitioner and to the Securities & Exchange Commission?

6. Did the District Court err in relegating petitioner to a straight bankruptcy petition?

7. Did the Court of Appeals err in affirming the District Court under the misapprehension that petitioner had proposed no plan of reorganization with its application for initial approval, and because petitioner had failed to submit evidence or assurance of additional available funds?

Statement of Matters Involved

On or about April 8, 1958, the petitioner filed a petition for relief pursuant to Chapter XI of the Act of Congress relating to Bankruptcy. On August 29th, 1958, an order was made by the Referee in Bankruptcy adjudicating the petitioner a bankrupt and directing that bankruptcy pro-

ceedings continue accordingly. Petitioner substituted counsel and on September 22nd, 1958 filed a petition for reorganization pursuant to Chapter X of the Act of Congress relating to Bankruptcy, together with proper affidavits in compliance with the rules of the United States District Court for the Southern District of New York (44-63). The bankruptcy proceedings were stayed by order of the Court pending the approval or dismissal of the petition upon certain conditions, with which petitioner complied to wit, the obtaining of a policy of insurance on machinery in the sum of $100,000.

Upon motion made by respondent herein, a purported creditor who had as yet filed no claim and whose attorney had not filed the affidavit required by said Chapter X, the Court below on October 28th, 1958, dismissed the petitioner's petition for relief pursuant to Chapter X. The Court made its decision summarily from the bench, without taking any evidence and without reading all of petitioner's papers but after hearing argument of counsel. On appeal to the United States Court of Appeals for the Second Circuit from the order of dismissal, the latter was reversed on the ground that the lower Court had made no findings of fact and that there was apparently no evidence showing the petitioner's financial condition or prospects, and the Court of Appeals remanded the action with directions that the Court should make adequate findings after taking evidence (261 F. 2d 560, 2nd Cir., November 20th, 1958).

The Court below upon the remand directed counsel for the petitioner to send out a notice of a hearing (205-206) directed only to the attorney for the objecting creditor and the trustee in bankruptcy stating that a hearing would be held "upon the issues raised by the motion of Sidney Liebernian."

At this hearing there appeared the trustee in bankruptcy, the attorney for the objecting creditor, the attorney for one secured creditor and an attorney representing a group of unsecured creditors, as well as counsel for the petitioner and its president. All except the adverse parties were permitted to intervene as friends of the Court. The Court inquired of the counsel for the petitioner whether there was any person who was then ready, able and willing to put money in the petitioner if the Court approved the petition.

Some inconclusive colloquy ensued (minutes of hearing of February 10, 1959, pp. 20-21), in the course of which, doubtless because of misunderstanding or inadvertence, the Court declared that the willingness of anybody "to put money in" if the petition should be approved was not evidenced by any writing; that the petition was "not filed in good faith"; and that a witness would be put on the stand "solely to give * * * an opportunity to make a complete record for the purposes of appeal."

Needless to say, after this abortive ruling, the extensive testimony of petitioner's president naming various corporations and individuals willing to supply capital (Minutes, pp. 24-25, 30) fell upon deaf ears. Nor did the Court, it is believed, trouble to examine such documents attached to the moving papers as the letter from the responsible head of Waggener Store Company expressing his willingness to advance $50,000 in cash to discharge petitioner's obligations. Another written overture was that of Charles S. Fields, Inc., which stated it was very much interested in supplying capital not only to pay off creditors but also for production.

Unfortunately, the error was compounded in that the foregoing written offers, along with a mass of other pertinent data, all comprising the petition for review in the District Court, with exhibits attached, fully establishing

petitioner's good faith were through oversight omitted from the record on appeal to the Court of Appeals, and were presented to that Court for the first time on the application for rehearing.

After the witness had concluded his testimony and notwithstanding the objection of the attorney representing unsecured creditors, the Court from the bench dismissed the petition of petitioner for relief pursuant to Chapter X. The appeal taken from the order and judgment of dismissal resulted in an affirmance by the United States Court of Appeals for the Second Circuit, and the denial of rehearing despite the submission of the omitted data.

Affidavits filed in support of the petition for reorganization by the petitioner herein pursuant to Rule X-4 of the United States District Court for the Southern District of New York set forth the financial condition and the stock structure and holdings of the petitioner. These matters, in brief, were as follows: Petitioner was initially incorporated to issue 500,000 shares of common stock, one class, par value 25¢ per share. Thereafter by amendment an additional 500,000 shares were authorized. After appropriate registration with the Securities & Exchange Commission a public offering was made at $2.00 per share. Of approximately 469,000 shares outstanding, 70% thereof is held by the general public, who purchased the same from the underwriters. These 70% represent about 400 stockholders widely scattered throughout the United States. Assets of the petitioner are not less than $591,315.78 and liabilities are $173,522.16. Fixed assets are in the sum of $247,238.31, which are included in the assets mentioned. Of these liabilities, $37,000 represents claims made by the petitioner's president for sums advanced by him and also due pursuant to a contract of employment; of the other liabilities petitioner disputes approximately $50,000. There is presently pend-

ing in the Supreme Court of the State of New York an action brought by petitioner in the sum of $571,000 for breach of a contract by the defendant therein, of petitioner, including $225,000 owed to petitioner.

The business of the appellant is the reprocessing of scrap and waste leather and the economical manufacture thereof by secret processes and formulae (patent pending with 19 claims allowed) into rolls of leather of such quality as to be practically indistinguishable from natural leather and appropriate for use in all industries using leather. The petitioner's main plant is at Sidney, Ohio, and consists of a brick building of approximately 50,000 square feet with four stories in front and three in the rear, with basement and sprinkler system. This plant contains machinery and equipment adapted to mass production of leather in continuous rolls. The original cost of the equipment at the plant is $152,271.69. At the time the plant was purchased in 1955 there was already in the plant approximately $275,000 of equipment and installations. The present replacement value of the plant is in excess of one half million dollars. The equipment is free and clear, with the exception of approximately $6,000 owed on a conditional bill of sale.

The main secured creditor of the petitioner is the holder of an Ohio type land contract. The contract is in the sum of $69,500, of which some $15,000 has already been paid by petitioner. A suit in equity in the State Court of Ohio in the nature of a foreclosure is presently pending.

Unsecured creditors are geographically scattered throughout the United States in some seventeen states and twenty-six cities.

Reasons for Granting Writ

A) The Court of Appeals has rendered an opinion in conflict with the opinions of other Courts of Appeals on the same subject.

B) The rulings of the District Judge and Court of Appeals are in conflict with the requirements of Title 11 Chapter 10 of the United States Code particularly Section 546 thereof.

C) The opinion of the Court of Appeals appears to be in conflict with an opinion of this Court on a similar matter.

D) The opinion of the Court of Appeals sanctioned a departure from the accepted and usual course of judicial proceedings by the District Judge which appears to call for the exercise of supervision by this Court.

E) The questions presented relate to corporate reorganization and are of a character frequently arising, so as to render clarification of the pertinent law desirable. Moreover, they involve the preservation of American business enterprises and are of widespread interest and vital importance.

ARGUMENT

Question No. 1

Was there any justification for the ruling that reorganization of the petitioner was not sought in good faith?

11 U. S. Code, Sec. 546 indicates some of the criteria for "good faith" in the approval of a petition for reorganization pursuant to said Chapter X. Nowhere in that section is there any requirement that the petitioner show that there is need for relief pursuant to *Chapter X*; that a plan of reorganization is "possible or feasible" or that there be produced upon the initial application for approval a person ready, willing and able to make an investment in the petitioner's business to consummate a plan for reorganization. As is succinctly stated in Collier on Bankruptcy, 14th ed., Vol. 6, at pages 1780 and 1781:

> " * * * it is unnecessary that the petitioner or petitioners at the outset prove the fairness, feasibility or equity of any particular plan or possible plans. Whether a plan is feasible * * * is a subject for subsequent inquiry and determination, after a trustee has investigated the debtor's financial condition, business and desirability of continuance thereof, has given the creditors and stockholders an opportunity to submit suggestions to a plan, § 167, and has submitted to the Court his own conclusions upon the subject."

Effective approval or disapproval of a plan must await the actual presentation of a proper plan and must follow a course marked out by the statute. To compel petitioner to submit a plan with its petition for reorganization would negate the plain intent of the Act, which provides that the

trustee initiate the proposed plan and that hearings be held with respect to the proposed plan or the inability to submit a plan of reorganization. See *Re 325 E. 72 St.*, 53 F. Supp. 997.

The District Judge's erroneous application of the law appears from his statement (Minutes, p. 72):

> "Unless money is put up, unless I can see there is a prospect of a settlement going through, I am not going to lend myself to an approval of this Chapter X."

The District Judge's summary holding that no plan was "possible" or "feasible" was clearly not a statutory criterion indicated in Sec. 546.

As was shown in the discussion (Minutes, pp. 14-15), this case presented a typical instance "where Chapter X affords a more adequate remedy than Chapter XI." Mr. Justice Douglas in *General Stores Corp. v. Shlensky*, 350 U. S. 462, 467.

Question No. 2

Was not the inability of petitioner to obtain relief under Chapter XI a compelling additional ground for initial approval of the petition?

The case last cited compels the conclusion that petitioner's failure to obtain relief under Chapter XI, providing for arrangements, was a most persuasive reason for invoking Chapter X.

The problem of the secured creditor, coupled with the widespread dispersion of the unsecured creditors and with the public holdings of petitioner's stock, patently rendered any arrangement impractical.

Chapter XI by its very terms is limited to "unsecured debts" (11 United States Code, Sec. 706, subd. 1), although the District Court apparently labored under the misapprehension that that Chapter permitted the adjustment of secured creditors' claims (Minutes, pp. 14-15).

Question No. 3

Was there any justification for the inference of the District Court that reorganization necessarily involved a public sale of stock?

In connection with this point, it may be observed at the outset that there is no law or, as far as can be ascertained, no authority barring reorganization through the sale of stock. Were such the plan, condemnation thereof would not *ipso facto* follow. It so happens, however, that no such project was contemplated.

For no reason whatsoever the District Judge conceived the idea that this was the intention of those interested, for he declared in no uncertain language (Minutes, pp. 46, 71):

> "I am not going to have you peddle more stock to the public with judicial approval * * *
>
> "It is apparent that you want to or your client wants to get refinancing by a second public offering."

This was his belief despite the testimony under oath to the contrary (*ibid.*, p. 72).

A ruling so manifestly predicated on no evidence at all should not be permitted to stand.

Question No. 4

Did the District Court err in deciding the issues prior to the hearing of witnesses?

As has already been shown in the recital of proceedings, the learned District Judge announced his intention to disapprove the petition before any witness had taken the stand and before any proof was offered. The taking of testimony thereafter, the Judge ruled, would be for the sole purpose of affording "an opportunity to make a complete record for the purposes of appeal" (Minutes, p. 20).

Such procedure, it is respectfully urged, does not constitute either a valid exercise of discretion or a just determination. It is violative of the time-honored Baconian precept: "Let not the judge meet the cause half way, nor give occasion for the party to say his counsel or proofs were not heard." In declaring his abortive ruling, the Judge made it abundantly plain that nothing could be adduced to alter the view he had adopted *in limine*, regardless of the absence of proof to sustain it. A judicial verdict in advance of any evidence is surely not calculated to produce the most comprehensive presentation where counsel and litigants understand that they are engaging in an idle ceremony. The hearing required by the statute is designed to produce a just result and is not a rite intended to establish a record for appeal. The petitioner is entitled to a decision on the merits and one that is the product of a true judicial discretion. The holdings below have sanctioned an arrant deprivation of that right, to the point of calling for this Court's supervision.

Question No. 5

Did the District Court err in failing to direct notice of hearing to all creditors, stockholders of petitioner and to the Securities & Exchange Commission?

The naked assertion of a single purported creditor that the petition was not submitted in good faith sufficed to result in its rejection. By way of contrast, the proposed plan met with the approval of the majority of creditors in number and amount, and their counsel excepted to the dismissal (Minutes, pp. 2-5, 81-82). The travesty of hearing (which actually followed rather than preceded the holding) was without notice to all other creditors of like class, without notice to the stockholders of petitioner and without notice to the Securities & Exchange Commission. The procedure was unauthorized (11 United States Code, Secs. 537, 561), and in no event was proper upon an initial application; issues as to final approval might have been raised by the filing of an answer by a person authorized to do so after initial approval.

Question No. 6

Did the District Court err in relegating petitioner to a straight bankruptcy proceeding?

The District Court ruled that bankruptcy could "accomplish what is desired here" (Minutes, p. 71). It was and is evident that such a course would result in the complete obliteration of the rights of the 400 stockholders. The good faith of the petition in such circumstances was required to be viewed in the light of whether "the interests of creditors and stockholders would be best subserved in such prior proceeding." The mention of stockholders is

especially stressed in the foregoing language which we quote from 11 United States Code, Sec. 541, subd. 4.

Question No. 7

Did the Court of Appeals err in affirming the District Court under the misapprehension that petitioner had proposed no plan of reorganization with its application for initial approval, and because petitioner had failed to submit evidence or assurance of additional available funds?

So far as the second phase of the above question is concerned, it is quite likely that the conclusion of the Court of Appeals was based upon the inadvertent omission of certain important documents from the record on appeal. This has been discussed in the statement, *supra*. Ample proof was adduced that responsible parties were prepared to come forward with the necessary funds.

Apart from the foregoing, it is submitted that the Court of Appeals adopted an erroneous view of the applicable law.

The holding is at variance with the Third Circuit in *Re Julius Rochrs Co.* (C. A. 3, 1940), 115 F. 2d 723, and with the Ninth Circuit in *White* v. *Penelas Mining Co.* (C. A. 9, 1939), 105 F. 2d 726; indeed, it is scarcely consistent with the Second Circuit's own decision in *Re Castle Beach Apartments* (C. A. 2, 1940), 113 F. 2d 762.

CONCLUSION

For all of the foregoing reasons, the petition for certiorari should be granted.

Respectfully submitted,

JACOB W. FRIEDMAN,
Attorney for Petitioner.

BERNARD J. COVEN,
Of Counsel.

Dated, New York, N. Y., September 14, 1959.

APPENDIX

Opinion of the United States Court of Appeals

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 329—October Term, 1958.

(Argued April 8, 1959 Decided June 29, 1959.)

Docket No. 25590

LEATHERHIDE INDUSTRIES, INC.,

Debtor-Appellant,

—v.—

SIDNEY LIEBERMAN,

Objecting Creditor-Appellee.

Before:

HINCKS, LUMBARD and WATERMAN,

Circuit Judges.

Debtor appeals from dismissal below, Southern District of New York, Ryan, *Ch.J.*, of its petition under Chapter X of the Bankruptcy Act. Affirmed.

BERNARD J. COVEN, New York City, *for Appellant.*

LOUIS P. ROSENBERG (Alfred A. Rosenberg, of counsel), Brooklyn, N. Y., *for Appellee.*

PER CURIAM:

On April 8, 1958 debtor filed a petition for an arrangement under Chapter XI of the Bankruptcy Act. A proposed arrangement was not accepted at a duly notified meeting of creditors, and, after the Referee on August 29 adjudged debtor bankrupt and directed it to proceed in bankruptcy, debtor then, within a month, filed a petition under Chapter X seeking a corporate reorganization. This Chapter X petition having been dismissed by the district court, debtor appealed to us. We remanded the action because at that time the record disclosed that the court below had not made adequate findings to support its dismissal order, *Leatherhide Industries, Inc.* v. *Lieberman*, 261 F.2d 560 (2 Cir. Nov. 20, 1958). The case is now once more before us. Upon remand the district court adhered to its former disposition. This time it spelled out its findings that debtor had proposed no plan of reorganization that was either possible or feasible, and it also found that the Chapter X petition was not filed by the debtor in good faith.

The findings of fact upon which the court below predicated its present order of dismissal are clearly correct. There is no evidence or assurance of any commitment by anyone that any additional capital funds are legitimately available to justify a court's certificate of approval of a reorganization. The pending bankruptcy proceedings initiated by the Chapter XI petition should go forward without further delay.

Affirmed.

Judgment

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the twenty ninth day of June, one thousand nine hundred and fifty nine.

PRESENT:

HON. CARROLL C. HINCKS,
HON. J. EDWARD LUMBARD,
HON. STERRY R. WATERMAN,

Circuit Judges.

LEATHERHIDE INDUSTRIES, INC.,

Debtor-Appellant,

—v.—

SIDNEY LIEBERMAN,

Objecting Creditor-Appellee.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is affirmed

A. DANIEL FUSARO
Clerk